***Gottesman & Co. v. Commissioner, 77 T. C. 1149 (1981)***

When consolidated return regulations are ambiguous regarding the calculation of accumulated taxable income for the accumulated earnings tax, the ambiguity must be construed against the IRS.

**Summary**

In Gottesman & Co. v. Commissioner, the U. S. Tax Court addressed whether consolidated return regulations mandated a consolidated or separate calculation of accumulated taxable income for the accumulated earnings tax. The IRS argued for a consolidated approach, but the court found the regulations ambiguous due to the lack of a clear method for calculating consolidated accumulated taxable income. The court ruled that this ambiguity should be construed against the IRS, favoring the taxpayer's interpretation of separate calculations. This case highlights the importance of clear regulatory guidance, especially for penalty taxes like the accumulated earnings tax.

**Facts**

Gottesman & Company, Inc. , the parent corporation of an affiliated group, filed consolidated returns for the tax years 1973, 1974, and 1975. The IRS determined deficiencies in Gottesman's income tax, asserting that accumulated taxable income should be computed on a consolidated basis for the accumulated earnings tax. Gottesman argued that the regulations did not provide clear guidance on how to calculate accumulated taxable income on a consolidated basis and thus computed it separately, believing this was permissible under the regulations.

**Procedural History**

Gottesman filed a petition in the U. S. Tax Court challenging the IRS's determination. The court considered Gottesman's motion for partial summary judgment on the issue of whether the consolidated return regulations required a consolidated or separate calculation of accumulated taxable income. The IRS conceded that this issue could be resolved without further factual inquiry.

**Issue(s)**

1. Whether the consolidated return regulations required Gottesman to compute its accumulated taxable income on a consolidated basis for purposes of the accumulated earnings tax.
2. Whether, if a consolidated calculation was required, the regulations provided an adequate method for determining accumulated taxable income on a consolidated basis.

**Holding**

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1. No, because the consolidated return regulations were ambiguous and did not clearly mandate a consolidated calculation of accumulated taxable income.
2. No, because the regulations failed to provide a method for calculating consolidated accumulated taxable income, leaving taxpayers without sufficient guidance to comply with the accumulated earnings tax.

**Court's Reasoning**

The court analyzed the history of the consolidated return regulations, noting that prior to 1966, a consolidated calculation was clearly required. However, the 1966 regulations removed the method for calculating consolidated accumulated taxable income, leaving only a reference to "consolidated accumulated taxable income" without a definition or calculation method. The court found this omission significant, especially since the accumulated earnings tax is a penalty tax that must be strictly construed. The IRS's subsequent proposals in 1968 and 1979 to define consolidated accumulated taxable income were withdrawn, further contributing to the ambiguity. The court concluded that Gottesman's interpretation of the regulations as allowing for separate calculations was reasonable under the circumstances. The court emphasized that the ambiguity in the regulations, which was of the IRS's making, must be resolved against the IRS.

**Practical Implications**

This decision underscores the need for clear regulatory guidance, particularly for penalty taxes. Taxpayers and practitioners must be cautious when interpreting ambiguous regulations, as the court may construe such ambiguity against the IRS. In practice, this case suggests that when regulations are unclear, taxpayers should consider alternative interpretations that favor their position, especially when dealing with penalty taxes. The ruling may encourage the IRS to provide more definitive regulations in the future to avoid similar disputes. Subsequent cases involving ambiguous regulations may reference Gottesman as a precedent for construing ambiguity against the taxing authority.

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